DOCUMENT RESUME

ED 413 474 CE 075 084

AUTHOR Walwei, Ulrich
TITLE Flexibility of Employment Relationships: Possibilities and Limits. IAB Labour Market Research Topics No. 22.
INSTITUTION Institute of Employment Research, Nurenberg (Germany).
ISSN ISSN-0945-8093
PUB DATE 1997-00-00
NOTE 20p.
PUB TYPE Reports - Research (143)
EDRS PRICE MF01/PC01 Plus Postage.
DESCRIPTORS *Employer Employee Relationship; Employment; *Employment Practices; *Flexible Working Hours; Foreign Countries; Job Development; Job Layoff; Job Sharing; Labor Legislation; Labor Market; *Organizational Development; Personnel Management; Personnel Policy; Public Policy; Scope of Bargaining; Wages; *Working Hours
IDENTIFIERS *Germany; Social Security

ABSTRACT

The controversial discussion of "atypical" forms of employment overlooks the fact that all parties involved can benefit from greater flexibility in the employment relationship. It all depends on what is made more flexible and how this greater flexibility is achieved. Employment relationships are built on a variety of factors (remuneration, operating hours, working time, and employment security). In principle, stability in one area of employer/worker relations (e.g., dismissal protection) demands flexibility in other areas (e.g., working hours or wages). Increased flexibility of working hours can create the potential for flexible models of annual working time by reducing or avoiding overtime or for creation of new part-time jobs. More scope for wage flexibility would enable a subtly differentiated adjustment of wage costs, oriented toward employment objectives. A possible starting point for this would be in profit-related remuneration components. Wage-dependent social security contributions could be limited to relieve the costs of the work factor by financing social security more from taxes. Laws regulating atypical employment relationships should help promote the creation of desired, voluntary atypical employment agreements but preclude any agreements being entered into on a nonvoluntary basis or limit the number of reasonable exceptions. (YLB)

****
* Reproductions supplied by EDRS are the best that can be made *
* from the original document. *
****

ED 413 474

IAB labour market research topics

No. 22

Institut für Arbeitsmarkt- und Berufsforschung

Institute for Employment Research

Ulrich Walwei

Flexibility of Employment Relationships:

Possibilities and Limits

U.S. DEPARTMENT OF EDUCATION
Office of Educational Research and Improvement
EDUCATIONAL RESOURCES INFORMATION CENTER (ERIC)
☐ This document has been reproduced as received from the person or organization originating it.
☐ Minor changes have been made to improve reproduction quality.
• Points of view or opinions stated in this document do not necessarily represent official OERI position or policy.

PERMISSION TO REPRODUCE AND DISSEMINATE THIS MATERIAL HAS BEEN GRANTED BY

T Rhein

TO THE EDUCATIONAL RESOURCES INFORMATION CENTER (ERIC)

- Employment Security
- Wage Policy
- Working-Time Policy
- Social Security
- Atypical Forms of Employment

1997

BEST COPY AVAILABLE

Institut für Arbeitsmarkt- und Berufsforschung
der Bundesanstalt für Arbeit
Regensburger Straße 104, D-90327 Nürnberg

CS 075 084

Publisher of the series:
Institut für Arbeitsmarkt- und Berufsforschung der Bundesanstalt für Arbeit (IAB),
Regensburger Strasse 104, 90327 Nürnberg/Germany
Telephone: +49-911-179-0
Telefax: +49-911-179-3258

Coordinators:
IAB Topics Working Group: Lutz Bellmann, Werner Dostal, Knut Emmerich, Barbara Koller, Gerhard Kühlewind, Gerd Peters, Hannelore Plicht, Thomas Rhein, Ulrich Walwei, Heinz Werner

Translator and editor:
Elke Limberger-Katsumi, c/o Institut für Arbeitsmarkt- und Berufsforschung der Bundesanstalt für Arbeit (IAB), Regensburger Strasse 104, 90327 Nürnberg

Distribution:
To order apply to the IAB, Regensburger Strasse 104, 90327 Nürnberg

Annual price:
DM 30 (for German subscribers); foreign subscribers are currently supplied free of charge

Copyright:
No part of this publication may be reproduced in any form without prior written permission of the IAB and in all reproductions full reference of the details must be given.

The series "IAB Labour Market Research Topics" is designed for the publication of selected papers resulting from the work done by the IAB or by studies commissioned by the IAB. Papers bearing the author's name do not necessarily represent the opinion of the IAB or the Bundesanstalt für Arbeit.

ISSN 0945-8093

Visit our Web Site at **http://www.iab.de**
with an English-Language-Section including
IAB Topics in full-text (as .PDF files)

The IAB is the research division of the German Bundesanstalt für Arbeit where scientists of different economic and social science disciplines work. The range of research topics can be characterized briefly as follows:
- observation of and forecasts for the German labour market
- labour market statistics
- labour market theory and policy
- evaluation of employment programmes
- regional and international labour markets
- occupation sociology
- research in skills and qualifications
- technological development and the labour market
- business and personnel management

BEST COPY AVAILABLE

Ulrich Walwei *)

FLEXIBILITY OF EMPLOYMENT RELATIONSHIPS: POSSIBILITIES AND LIMITS

0 Abstract

1 How flexible or rigid are employment relationships?

2 Employment security as a brake on flexibility?

3 Can flexible working-time bring about an employment miracle?

4 Employment security through wage concessions?

5 Is social security an employment trap?

6 Atypical forms of employment: integration vs. exclusion?

*) Researcher of the Institut für Arbeitsmarkt- und Berufsforschung

0 **Abstract**

1. In view of the severe employment crisis in the European industrial countries, the subject of labour market flexibility is increasingly becoming the focus of public attention. A possible need for flexibility is, however, not only to be seen in the fields of labour costs, working hours and legal employment protection, but also with respect to functional aspects such as the mobility of employees within a company or the necessary aspect of passing on knowledge and abilities.

2. Wages policy must surrender more to its responsibility in employment policy issues. More scope for wage flexibility legitimised by the social partners would be desirable, as this would facilitate a subtly differentiated adjustment of wage costs, orientated towards employment objectives, in cases when a company experiences economic difficulties due to cyclical and/or structural changes. A possible starting point for this would be in particular profit-related remuneration components, which could be made use of more frequently. In addition, it concerns measures for limiting the wage-dependent social security contributions and therefore for relieving the costs of the work factor (by financing social security more from taxes).

3. An issue of particular interest with regard to employment policy is the combination of increased flexibility of working hours and reductions in working hours. Increased flexibility of working hours can create considerable potential for employment creating measures of reductions in working hours. There would be potential for such reductions in the introduction of innovative shift models with regard to the working week, in the use of flexible models of annual working time by reducing or even avoiding overtime, or in the extension of operating hours by creating new part-time jobs.

4. The relationship between stability and flexibility in the employment system can be clarified using the example of protection against dismissal. Here it must be taken into consideration in principle that stability in one area of employer/worker relations, e.g. in the form of dismissal protection, demands flexibility in other areas, e.g. with regard to working hours and/or wages. In this respect completely inflexible employer/worker relations would have fatal consequences with regard to employment policy. On the other hand it must be considered that other areas of flexibility, e.g. a multifunctional use of workers, require stable basis conditions.

5. 'Atypical employment' (e.g. part-time work, working out of the home, temporary work) can, but need not necessarily, have a precarious character. In this respect banning such employment would be absurd and unnatural. In modern industrial societies what matters is that the institutional framework supports or at least does not hinder the materialisation of the desired voluntary arrangement of atypical forms of employment. An important precondition for this would be placing the workers in atypical employment on an equal legal footing with the 'normal' workers as far as is possible. The principle is therefore not one of exclusion, but one of the greatest possible degree of integration of these employment forms into the employment system as a bridge to 'normal' employment.

BEST COPY AVAILABLE

6. In principle the flexibility of employment relationships is a necessary precondition for firms and workers being able to adapt to changing challenges within and outside the company, so that existing employment relationships can be reorganised or dissolved and re-established. Here it cannot be simply a matter of maximum labour market flexibility in general, but a matter of well considered modernisation of the institutions and regulations which affect the labour market.

1 How flexible or rigid are employment relationships?

There is empirical evidence that more people today are working in part-time jobs, that many new employment contracts are fixed-term contracts, and that firms are tending to hire more agency staff or to outsource to self-employed workers in order to avoid employment risks, (see also the trend reflected in table 1). These trends give rise to hopes or fears, depending on perspective. However, the rather controversial discussion on 'atypical' forms of employment overlooks the fact that all parties involved can benefit from greater employment relationship flexibility. It all depends on what is actually made more flexible and how this greater flexibility is achieved.

The labour market can be made flexible both on a macroeconomic level and a microeconomic level. On the macroeconomic level, *flexible* simply describes the nature of the employment system and the way it is working. We may say that there is *flexibility* on the macroeconomic level when the labour market is balanced. However, a balanced labour market does not mean that supply and demand of labour have to balance each other out permanently. Seeking employment and filling a vacancy always take some time: thus frictional unemployment is always associated with a certain number of unfilled vacancies and unemployed workers. Moreover, the labour market is subject to the economy's normal fluctuations, which can lead to unemployment in time of recession and to general and skilled labour shortages during an economic upswing.

However, the labour market will not be able to function on the macroeconomic level if there are structural deficits. Examples may be high unemployment over a long period, as is the case in many industrialised countries in Europe, or an acute shortage of skilled labour as a result of an overall labour shortage or a shortage of manpower with specific qualifications. There is general agreement that the macroeconomic flexibility of the employment system has to be improved. There is no agreement, however, on how to achieve this.

It is often said that greater flexibility on a microeconomic level would help to solve macroeconomic problems. Such flexibility would inherently entail a willingness on the part of firms to adapt their human resources policies, as well as the definition of the essential needs of employees (or job seekers). The central issues in the discussion about creating a more flexible system are thus: How flexible do employment relationships have to be on the microeconomic level without either creating or compounding problems on the macroeconomic level? How can flexibility be achieved on the microeconomic level without creating any social problems and conflict?

BEST COPY AVAILABLE

Table 1: Non-standard Forms of Employment in European Union Countries – (1983–1995)

	Temporary work [1]			Part-time employment [2]			Self employment [3]		
	% 1983	% 1995	Diff. 95/83	% 1983	% 1995	Diff. 95/83	% 1983	%1995	Diff. 95/83
Belgium	5.4	5.3	–0.1	8.1	15.4	7.3	14.7	15.4	0.7
Denmark	12.5 [5]	12.1	–0.4	23.8	22.5	–1.3	11.6	8.4	–3.2
Germany [4]	9.9 [5]	10.4	0.5	12.6	16.4	3.8	9.0	9.4	0.4
Greece	16.3	10.2	–6.1	6.5	3.4	–3.1	36.5	33.8	–2.7
Spain		35.0			7.1			21.8	
France	3.3	12.3	9.0	9.7	16.2	6.5	-12.8	11.6	–1.2
Ireland	6.1	10.2	4.1	6.7	13.3	6.6	21.3	20.8	–0.5
Italy	6.6	7.2	0.6	4.6	6.1	1.5	23.9	24.5	0.6
Luxemburg	2.4	2.7 [6]	0.3 [7]	6.7	8.0	1.3	9.5	10.0	0.5
Netherlands	5.8	10.9	5.1	21.2	37.4	16.2	9.5	11.5	2.0
Portugal		10.0			4.4			25.8	
United Kingdom	5.5	7.0	1.5	19.0	24.5	5.5	10.2	13.0	2.8

1) Temporary workers as a ratio of all dependently employed persons. Includes employees in training relationships as well as agency staff
2) Part-time employed as a ratio of gainfully employed persons.
3) Self-employed persons as a ratio of gainfully employed persons
4) All figures for 1983 refer to West Germany, those for 1995 refer to Germany as a whole.
5) Data refer to 1984.
6) Data refer to 1994.
7) Data refer to 1994/1983

Source: Eurostat, Labour Force Statistics, 1983 & 1995 Luxemburg; Labour Force Survey 1983 & 1995

BEST COPY AVAILABLE

These goals require a clear definition of the concept of flexibility of employment relationships. Employment relationships are built on a variety of factors, (e.g. remuneration, working-time, employment security). The package of conditions governing the different components of an employment relationship are specified in individual contracts, collective agreements and laws. Such conditions can be regarded as either flexible or rigid (see table below):

Table 2: Flexibility of Employment Relationship Factor

Flexible <-------	Employment relationship factor	-------> Rigid
profit-related	remuneration	non profit-related
working-time independent of firm's operating hours	operating hours	working-time determined by operating hours
possibility of part-time work and overtime	length of working-time	fixed weekly working-time
right of either party to terminate employment relationship	employment security	workers cannot be dismissed

This table shows how different employment relationship factors may be more or less flexible. From an economic point of view, clearly not all factors can be rigid at the same time. However, the question is: just how flexible should or can employment relationships be? The rest of this paper discusses the potential of and limits to increasing the labour market's flexibility by examining the factors that go to make up employment relationships, and suggests possible consequences.

2 Employment security as a brake on flexibility?

Employment security does not necessarily imply legal protection against dismissal. It is very obvious that certain employees (e.g. in certain small firms) in fact enjoy a high degree of employment security without any formal regulations; legal protection against dismissal, however, does not provide absolute security of employment. It simply means that there is economically viable dismissal protection in place to prevent arbitrary lay-offs. Employers must therefore justify redundancies on objective grounds and respect certain procedures (e.g. giving notice).[1]

[1] For details see: Büchtemann, Christoph and Walwei, Ulrich: Employment Security and Dismissal Protection, in: Schmid, G. et al., International Handbook of Labour Market Policy and Evaluation, Cheltenham and Brookfield, 1996, S. 594-622

BEST COPY AVAILABLE

Employment security is one of the central factors in an employment relationship. The example of dismissal protection shows that not all factors of an employment relationship must or should be flexible at the same time. Flexibility in one area may offset an absence of flexibility in others. For example, a high degree of employment security may offset more flexible working hours or wages. On the other hand, certain types of flexibility require a general framework of stable conditions. While dismissal protection limits 'quantitative' manpower flexibility, it nevertheless creates a framework for the future, where employees are able to be flexible, adapting to new demands and tasks that need to be performed (e.g. by accepting mobility within the firm or technical innovation). This in turn means that investment in human resources can have a positive effect on productivity.

Excessive dismissal protection can become counter-productive, however, when employment relationship conditions, although satisfactory for the parties directly involved, have negative consequences for third parties. When there is general under-employment with a high degree of employment stability and little labour turnover, it becomes more difficult for the unemployed to be integrated into the labour market. For example, exceptional protection measures (e.g. in cases such as the severely disabled in Germany, who enjoy special dismissal protection) might create categories of people who, despite the special protection they enjoy, run a higher risk of remaining unemployed. Dismissal protection may also fail when it can be circumvented. Overly extensive dismissal protection will encourage firms to opt mainly for all unprotected – or at least less protected – forms of employment (e.g. fixed-term contracts, the use of agency staff or outsourcing to self-employed persons).

To this day, discussions about atypical forms of employment are characterised by one-sided arguments. The advantages for companies of being able to introduce more atypical forms of employment as a result of deregulation have always been stacked up against the disadvantages for the employees. One camp argues that a lack of flexibility and the ensuing even higher cost of labour would discourage firms from taking people on. The opposite camp argues that labour would have to pay the price for increased flexibility, because wages, working conditions and social protection would be eroded in atypical forms of employment.

However, when looking at the changes in employment taking place worldwide, this line of argument seems to be too simplistic. Most firms still do not exploit the full (theoretical) potential of labour flexibility (e.g. by constant 'hiring and firing'). In practice, firms usually turn to various forms of atypical employment to obtain greater labour flexibility when they need to cut adaptation costs. Temporary forms of employment (agency staff, fixed-term contracts) also represent an important alternative or complementary source of staff, because they allow employers to try employees out without commitment and hence select better personnel.

In addition, the interests of employees are anything but homogeneous and cannot all be met by one particular type of employment. There has also been a general change in values, and now more people are attracted to atypical forms of employment for all sorts of different reasons, creating in the process a considerable labour supply for this kind of employment. A broad limitation on atypical forms of employment would therefore not be desirable from the perspective of the workforce in general. However, a distinction

BEST COPY AVAILABLE

must be made between where atypical forms of employment are the main gainful activity, and where they are a secondary occupation. Where it is the main activity, an atypical form of employment seems only to be attractive when it can act as a springboard to a career or a way out of (long-term) unemployment. Furthermore, it is mainly people who are interested in a non-continuous or less substantial (secondary) occupation who would consider taking up some form of atypical employment.

Bearing in mind that atypical employment is now an essential feature on today's labour market landscape, what implications does its growth have for employment policy? An analysis of the possible effects of an increase in temporary work on employment turns up no spectacular results. It is true that more temporary employment options might partly offset companies' restraint in hiring during an economic upturn. On the other hand, it would be easier to make staff redundant (i.e. when temporary employment contracts run out) at times of economic stagnation. Overall, this would not really increase the average rate of employment in the long run (e.g. through fewer hours of overtime). The only outcome would be a greater fluctuation in the labour market, which might at least improve the chances of those out of work to get a toehold on the market.

3 Can flexible working-time bring about an employment miracle?

A two-pronged strategy may be implemented to make working-time more flexible: by determining the hours when the work must be done (i.e. dissociating operating hours and working-hours) and by varying the length of individual working-time (i.e. reducing working-time in various ways). There is an economic reason for determining the times which are to be working-times more flexibly: this allows the firm to utilise its capacities better by lengthening the machine run times or by extending the service schedules (e.g. by more evening, shift, or weekend work). When firms dissociate operating hours from working-time, the unit cost of the required capital decreases (for existing capacities). A further advantage is that it is easier to adapt the number of workers employed. It is a well-known fact that firms are subjected to fluctuations in production or demand. With the help of flexible working-time, (e.g. in the form of annual or lifetime working-time accounts), working hours can be extended during times of substantial demand, or reduced during economic downturns. In this sense, flexible working-time models help reduce labour costs, because the additional overtime and the wage costs can be completely or partially avoided.

What seems to be most significant for employment policy is the combination of more flexible operating hours and working-time reduction measures. Working-time could potentially be reduced by introducing shift models for weekly working-time (e.g. by introducing 4 nine-hour shifts instead of 5 eight-hour shifts), by annual working-time models with little or no overtime at all, and by extending operating hours by creating new part-time jobs.

For quite some time, a single issue has dominated the European debate on working-time as the foremost employment policy option: the extension of part-time work.[2] More part-

---

[2] See Walwei, Ulrich and Werner, Heinz: More Part-time Work As a Cure for Unemployment? – Results of an International Comparison. IAB Labour Market Research Topics, no 16/1996

BEST COPY AVAILABLE

time work – so the argument runs – would permit more people to find work. However, the apparently inexorable growth of this form of employment not only has given rise to hopes but also to fears – which must be taken seriously.

More part-time work may reflect a change in employment relationships. It allows for a better combination of work and other activities, such as being with family, education, voluntary work and hobbies. It can also be seen as a bridge between two different stages in one's career: first-time job-seekers and people returning to work can be integrated more easily. Furthermore, part-time work at the end of one's working life can provide a smoother transition to retirement. However, an increase in part-time employment can also indicate that there are not enough employment alternatives and in particular full-time job opportunities.

The growth in part-time employment may also be symptomatic of a change in a company's labour policy. With the advent of more part-time work, labour capacities can be more flexibly adapted to production needs – or customer needs in the case of service industries. The flexible use of part-time workers can also save on costly overtime. However, part-time jobs may also serve other corporate labour policy objectives. For example, a firm may establish a long-term relationship with qualified skilled workers by granting them 'part-time training leave'. Also, crises caused by a decline in orders can be overcome more easily by temporarily increasing part-time labour. Finally, as has been pointed out time and time again, part-time staff are more productive than full-time staff. The main reasons cited for the higher productivity of part-time workers are that full-time staff suffer more fatigue and more absenteeism because of illness. There are, however, also reasons why firms make no or only minimal use of part-time manpower, e.g. the problems involved in dividing tasks to be shared, or the need for a greater degree of co-ordination and administration with larger numbers of staff.

From the perspective of the economy as a whole, the issue of expanding part-time work is controversial. Whenever there is a labour shortage, part-time work is seen as one possible means of increasing the labour supply (e.g. through people returning to work or retired persons). In times of recession, employment can be safeguarded by means of job-sharing, preventing an even greater increase in the number of unemployed. However, an increase in part-time work can also be accompanied by undesired side effects: a shortage of full-time jobs can create 'part-time unemployment'. This, in turn, can lead to phenomena such as the second or third job. Furthermore, enforced or involuntary part-time work may induce even more activity in the underground economy because people have more free time.

Promoting part-time work will require a sustained effort entailing behavioural change on the part of the players.[3] Another reason why part-time work should be expanded slowly is the problem of distributing the work between more people, i.e. balancing the qualifications offered and those in demand. Even where it might be economically feasible to share a position, the qualifications of the two or more jobsharers must first fit the job.

---

[3] For a detailed discussion see: Walwei, Ulrich and Werner, Heinz, ibid.

BEST COPY AVAILABLE

Part-time work cannot be viewed as a panacea that will bring about a sustained reduction of unemployment because it will probably increase rather slowly, and also because more part-time work means higher labour productivity, as companies' motivations for hiring part-timers indicate. If the average weekly working-time for newly created part-time jobs were to differ only slightly from that of full-time work relationships (which is what many employees want), the effect on the labour market within the economy as a whole and consequently the fall in unemployment would be quite small because of the resultant effect on productivity. If, on the other hand, the additional part-time jobs are quite different from full-time work, this would certainly lead to more employment, although this would really lead to drop in the 'silent reserve', and only a minor reduction in official unemployment figures. This can be seen quite clearly in the example of the Netherlands, part-time work world champions.

This is not to deny the usefulness of initiatives and campaigns aimed at promoting part-time employment. However, their main purpose is not so much to reduce unemployment but rather to create new jobs and safeguard existing jobs by offering employees a wider range of choices, by increasing the productivity of individual companies and the economy as a whole, and by reducing the 'silent reserve', a very desirable social policy objective. To a certain extent, a larger supply of part-time work can thus reduce the divide in society that separates those in employment and those without work.

4 Employment security through wage concessions?

The relationship between wages and employment is extremely complex. Yet the liberal approach offers a relatively simple explanation, defining unemployment mainly in terms of excessively high wages. This would mean that employment could only be increased, or unemployment reduced, by real wage decreases. The prerequisite for full employment would then be for wages to be established as freely as possible. Any impediment to the free determination of wages (e.g. national or collective minimum wage agreements) would be regarded as an obstacle to employment. This same approach says that particularly the problem groups on the labour market ('minimum wage unemployment') suffer from a lack of outside competition. Excessively high real wages could also contribute to low capital profitability and, consequently, to a lack of the kind of investment that creates employment ('capital-shortage unemployment').

Despite the superficial plausibility of this liberal point of view and its hypotheses, the prevailing doubts as to its overall validity are well-founded. New labour market theories (e.g. screening, transaction, contract and efficiency wage theories) specifically deal with the economic reasons for fixed minimum wages. The arguments can be summed up as follows: salaries above the actual market 'clearing rate' can sometimes even prove advantageous for companies. By offering attractive wages, firms can choose the most suitable employees from a larger and better pool of labour. They can keep turnover low by offering better salaries. And they can expect employees to be more willing to perform better in return for good wages. Empirical findings also warn against hasty recommendations aimed at a global wage reduction. Employment levels are the result of a variety of factors. In addition to high wages, factors such as domestic demand or foreign trade are also important. Otherwise, it would be impossible to explain why employment and wage never systematically correlate, confirming what is generally assumed to be the case. This is why expanding employment can go hand-in-hand with

BEST COPY AVAILABLE

an increase in real wages, and employment fluctuations are compatible with relatively steady wages. This also shows that wages are not only cost-effective but also demand-effective.

Unit wage costs are an important factor for evaluating international competitiveness: they are also very important as far as the level of employment is concerned. They go up whenever nominal wage increases outstrip the increase in productivity. It is irrelevant why this occurs, i.e. whether the unions are simply aiming to offset previous or current price increases, or whether they want to see a redistribution of income in favour of the workers. So, if nominal wage increases outstrip the productivity increase, higher unit wage costs not only cause higher prices, but may also cause unemployment. This is especially likely when continued price increases lead to a restrictive monetary policy. In the last two decades nearly all European industrialised countries have had good reason to attach great importance to the stability of price levels. However, this greater price stability was achieved at a cost: high unemployment and a chronic weakness in growth. In this sense, distribution aspects (beyond the conflict between capital and labour) play an important part in the present wage agreements. Therefore, either those already in employment would benefit from expected productivity increases in the form of higher wages, or the unemployed would benefit in the form of working-time reductions with or without full wage compensation.

The flexibility discussion focuses on the variability and differentiation of earned income as well. The gradual reduction in the differentiation of wage structures according to sector, location and qualifications in Europe is often criticised as having been one of the causes of higher structural unemployment. However, this much-criticised trend towards levelling out differences cannot always be demonstrated empirically.[4] Therefore, a proposition that might seem much more viable is to make existing wage structures even more flexible (e.g. by more decentralised negotiations or even by waivers).

More variable wages would be advantageous because they would permit an adjustment of wage costs when companies are faced with cyclical and/or structural problems. Similarly, during an economic boom, upward adjustments could be made more quickly and smoothly. More flexibility to adjust wage structures presupposes a social consensus, however. One could, for example, imagine a situation in which companies making losses would temporarily forego wage increases, with the proviso that there would be an increase as soon as they are making a profit again. Another way to increase wage flexibility would be to envisage more performance-related remuneration components (e.g. for work compensated at a higher rate than the agreed scale).

However, wage structure flexibility also affects the distribution of incomes. The advantage of a larger diversity of wages (e.g. as seen in the USA) is that there is a greater performance incentive and it is easier for the out-of-work to get into the labour market. A significant disadvantage is that many new jobs would probably pay incomes at or even below the poverty line (the 'working poor'). Partial waivers in the wage agreements

---

[4] See Franz, Wolfgang: Chancen und Risiken einer Flexibilisierung des Arbeitsrechts aus ökonomischer Sicht. <Economic opportunities and risks involved in increasing the flexibility of labour regulations.> Paper given at the research seminar on 'International labour market research' at the University of Constance, no 10/1993

BEST COPY AVAILABLE

might be a compromise. In order to facilitate the re-entry into the labour market of the long-term unemployed in particular, unions and management might agree on an even greater number of so-called 'newcomer wages'. Once the previously unemployed person has successfully been integrated into the workforce, he or she would then have to be paid at least the normal minimum wage.

5 Is social security an employment trap?

International comparisons of labour costs in the manufacturing industries put western European countries at the top of the league year after year.[5] However, the absolute cost of labour has only limited relevance as an indicator of competition, because taken by itself, it does not reveal what and how much is produced per unit of time. A more important factor for assessing competitiveness is unit wage costs trends, especially in comparison with rival national economies. But even relatively high unit wage costs, (which prevail in most European industrialised countries) would not, by themselves, be an obstacle to competition, if these higher labour costs are justified by the quality of the goods and services produced (including aspects such as reliable delivery, after-sales service, guaranteed spare-part replacement), something which is extremely difficult to measure objectively.

Given the high rate of unemployment, as well as the recent competition from cheap labour from south-east Asia and eastern Europe, the level and structure of labour costs are being put to the test in the industrialised countries of Europe. This is because from a macroeconomic perspective, wages and additional labour costs are the second most important cost factor after the price of imported goods. The relatively high level of labour costs in western Europe is caused in part by direct payments to employees (i.e. wages) followed by 'non-wage labour costs'. While employers' contributions to non-wage labour costs raises the cost of production, the employees' contributions reduce their net earnings. For this reason, employment policy suggests that top priority should be given to measures to reduce the wage-related non-wage costs in many European countries. If job creation and, in particular, the fight against 'structuralising' unemployment are to be given priority, then an overall reduction of non-wage labour costs is called for, since they increase overall labour costs. Also, a carefully considered reduction in contributions payable by low-paid workers would give fresh impetus to the creation of employment.[6] Rightly or wrongly, companies expect only below-average productivity contributions from the hard core long-term unemployed and others who are at a disadvantage on the labour market. More low-productivity jobs would therefore particularly benefit this category of workers. Exempting low-income earners from certain contributions (e.g. both for income tax and social insurance) would help compensate for the net income loss associated with a low gross wage. Social security contributions (e.g. pensions, health and unemployment) and the way they are financed largely explain the high non-wage labour costs.

---

[5] See, for example, Schröder, Christoph: Industrielle Arbeitskosten im internationalen Vergleich <An international comparison of industrial labour costs>, 1970-1995, in: iw-trends, vol. 2/1996

[6] See Bellmann, Lutz: Wage Differentiation and Long-term Unemployment - An International Comparison. IAB Labour Market Research Topics, no 19/1996

BEST COPY AVAILABLE

The central issue relating to the level of social security payments concerns which social risks should be borne by the community as a whole and which borne or shared by individuals. It would be worth exploring whether the government should fund a basic insurance scheme, particularly to cover retirement pensions and health insurance, and how much individuals should be expected to contribute. Another important question is whether all employees should be eligible for social insurance. In a good number of countries (e.g. Great Britain, Denmark and Germany) there are so-called 'eligibility thresholds'. As a consequence, part-time workers with very low incomes or very low (average) weekly working-times are partially or totally excluded from social security. This means that employees working only a small number of hours have to do without protection, although they do not have to make contributions (which would otherwise reduce their net income).

Assessments of what constitutes 'marginal' employment differ according to the perspective of the party involved in the labour market. 'Eligibility thresholds' generally mean lower labour costs for companies (since they are on a basis of one working hour compared to other employment relationships that are covered by social security), so such employment relationships could become more attractive. However, such positions are generally less acceptable to employees when they offer little social protection. Under certain conditions this can negatively affect the quality of the labour supply for such jobs and therefore a company's productivity. It should nevertheless be pointed out that the people working in such marginal jobs are often covered by other types of social insurance (e.g. married persons, pensioners, job-seekers and students). For this category of persons, the decisive factor in choosing a job is more the short-term, additional net income rather than social security coverage, since it is unnecessary. Therefore, it is important to be clear when appraising eligibility thresholds. If they are low, they may help to increase both the job opportunities and net earnings of workers who do not have a solid attachment to the labour market (e.g. students working part-time). If, on the other hand, the eligibility thresholds are rather high, they tend to discriminate against part-time workers who have demonstrated an on-going labour market attachment.

Another question is how a given level of social security is to be financed. Financing by employer and employee wage-based contributions as well as by direct or indirect taxation are alternative or complementary solutions one might want to consider. Social insurance systems which rely too much on contributions particularly risk putting excessive strain on labour costs and reducing the attractiveness of labour. Indirect taxes might be a way of providing fiscal policy compensation for exemption from wage-related social insurance contributions.[7] In its model calculations, the European Commission says that heavier taxation on energy consumption combined with exemptions from non-wage labour costs will benefit the labour market.[8]

---

[7] Simulations done by the Institut für Arbeitsmarkt- und Berufsforschung point to net employment effects of a re-financing of unemployment insurance in the form of increased mineral oil tax (see detailed discussion in the IAB Workshop Report, no. 5/10.9.1996: Wege zu mehr Beschäftigung – Simulationsrechnungen bis zum Jahr 2005 am Beispiel Westdeutschland)

[8] See European Commission: Growth, Competitiveness, Employment (White paper). Luxembourg and Brussels, 1993

BEST COPY AVAILABLE

6 Atypical forms of employment: integration vs. exclusion?

Both enterprises and labour need work relationships to be flexible in order to be able to adapt to changing demands inside and outside the company by modifying or terminating existing work relationships or creating new ones. However, the issue is not how to achieve maximum labour market flexibility as a whole, but rather how to modernise the employment system and improve the operation of the labour markets in a sustainable way.

Since atypical employment is probably not going to be the first choice for either companies or people looking for work, it is likely that the interests of the parties involved will sometimes coincide and sometimes not. When interests differ, the atypical forms of employment that finally come out of the process will largely depend on how far both contracting parties are prepared to make concessions. Clearly then, atypical forms of employment can be viewed as being good or bad, depending on perspective. Atypical employment can (but need not) be precarious. For this reason, barring it would be economically absurd and unrealistic.

Consequently, the law regulating atypical employment relationships has a complex role to play today. Firstly, the institutional framework should help promote – or at least should not hinder – the creation of desired, voluntary atypical employment agreements. An important condition for this is that workers in atypical employment should, as far as possible, be placed on a par with 'normal' employees. The underlying principle should be integration, not exclusion. Ending discrimination against these workers would help integrate 'atypical' forms of employment (such as part-time or temporary work) into 'normal' employment, which would not be particularly difficult, especially as these options are very promising for the future. Moreover, voluntary agreements could also be entered into more easily, (for example, in the area of fixed-term work contracts), if there were practicable, prescribed regulations establishing a clear legal framework. Voluntary agreements would also benefit if the legal framework were to leave the maximum possible latitude and flexibility appropriate for individual agreements (in particular, in the area of part-time work).

Another important role of social protection legislation is to try to preclude any agreements being entered into on a non-voluntary basis, (e.g. because of a lack of suitable alternatives), or at least to limit the number to a few reasonable exceptions, for example, recommending atypical employment forms to promote the reintegration of hard-to-place people, especially the long-term unemployed. Atypical forms of employment offer a wide range of alternatives to prevent the long-term unemployed being cut off completely from the labour market or to assist them re-establish their contact with it. For example, there is the Dutch 'Start' model: persons who are difficult to employ can work with non-profit agencies and be 'lent to' borrower firms who 'try them out'. An important factor to consider particularly in the case of creating part-time jobs for formerly unemployed persons, is that individuals on welfare must have a better chance to earn extra money and thus to reduce their dependence on such benefits. Another option is the provision of specific measures (e.g. in the form of advisory and support services) designed to assist people start their own business and get out of unemployment that way. The number of unemployed eligible for this kind of assistance should not be overestimated, though. Existing studies indicate that few (less than 5 %) of

BEST COPY AVAILABLE

unemployed persons would qualify.[9] Labour market policy should not expect the long-term unemployed to make the increasingly difficult leap into a normal work relationship: it should make careful use of atypical forms of employment to reduce – slowly but surely – the obstacles to their complete re-integration into the labour market.

BEST COPY AVAILABLE

[9] See OECD: The OECD Jobs Study. Evidence and Explanations, Paris 1994

The papers published in this series:

1 Ulrich Walwei, Heinz Werner:
Employment and Social Dimensions of the Single European Market (1993)

2 D. Bogai, F. Buttler, K. Emmerich, W. Klauder, M. Koller, G. Kühlewind, U. Möller:
Promoting Employment Instead of Financing Unemployment – Advocating an Investive Employment and Labour Policy in the New German States (1993)

3 Gerhard Kühlewind:
Long-Term Labour Market Projections – Methods and Results for the Federal Republic of Germany – (1993)

4 Manfred Tessaring :
Manpower Requirement By Levels Of Qualification In West Germany Until 2010; Implications of the 1989 IAB/Prognos Projection for the Qualification Structure of Jobs (1993)

5 Ulrich Walwei:
Monopoly or Coexistence: An International Comparison of Job Placement (1993)

6 Heinz Werner:
The Integration of Foreign Workers into the Labour Market, (France, Germany, Netherlands, Sweden) (1994)

7 Friedrich Buttler/UlrichWalwei:
The Employment Contract: Cooperation Requires Stability (1994)

8 Friedrich Buttler/Manfred Tessaring:
Human Capital as a Location Factor: Arguments for the Education Policy Discussion From a Labour Market Policy Standpoint (1994)

9 Barbara Koller
Social and Occupational Integration of Immigrants of German Origin in Germany (1994)

10 Gerhard Kühlewind
Gainful Employment and the Inter-Generational Contract (1995)

11 Johann Fuchs
Long-term Labour Force Projections for Germany – the Concept of Potential Labour Force – (1995)

12 Heinz Werner
Economic Integration and Migration: the European Case (1995)

BEST COPY AVAILABLE

The papers published in this series (continued):

13 Alfons Barth
IAB Long-term Labour Market Projections and Policy Simulation with the SYSIFO Macroeconometric Model – Concept and Application (1995)

14 Thomas Rhein
The European Monetary Union: Possible Consequences for Employment and Earnings (1995)

15 Lutz Bellman/Susanne Kohaut
Determinants of Wages in the German Service and Manufacturing Sectors: An Empricial Analysis Based on the IAB Establishment Panel (1995)

16 Ulrich Walwei/Heinz Werner
More Part-time Work as a Cure for Unemployment?
Results of an International Comparison (1996)

17 Ulrich Walwei
Placement as a Public Responsibility and as a Private Service
An International Comparative Perspective of the Reorganization of Placement Systems (1996)

18 Heinz Werner
Temporary Migration of Foreign Workers – Illustrated with Special Regard to East-West Migrations (1996)

19 Lutz Bellmann
Wage Differentiation and Long-term Unemployment – An International Comparison (1996)

20 Lutz Bellmann
The IAB Establishment Panel with an Exemplary Analysis of Employment Expectations (1997)

21 Werner Karr
Conceptual Problems in the Understatement of Long-term Unemployment (1997)

22 Ulrich Walwei
Flexibility of Employment Relationships: Possibilities and Limits (1997)